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SIPDIS

SENSITIVE

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SUBJECT: IMF REVIEW TEAM IN MALAWI

SUMMARY

1. (U) The International Monetary Fund's Staff Monitoring Program assessment team has briefed donor mission representatives twice since its arrival in Malawi. The team leader has characterized the GOM's performance as good through the end of September and outlined a scenario under which the Fund may start a new Poverty Reduction and Growth Facility by April. This preliminary assessment confirms our impression of Malawi's generally good fiscal performance since the current administration took office in May. End summary.

MEETING TARGETS BY A WIDE MARGIN

2. (U) In briefings on November 9 and November 17, the leader of the International Monetary Fund's (IMF) Staff Monitoring Program (SMP) assessment team John Green appraised Malawi's macroeconomic performance as "so far, so good." The team is assessing the GOM's performance through the end of September and will be in Malawi until 26 November. Before leaving the country, the team expects to issue an assessment letter and brief the press.

3. (U) The team considers Malawi to be meeting its targets "by a wide margin," the margin being due in part to delays in planned expenditures for commercial maize. Even after the maize buy, Malawi will still meet all quantitative targets. The country is reportedly on track for seven of its eight structural measures, with an agreement to delay the eighth (which concerns submission of outstanding check numbers to the Reserve Bank) until 1 December. Based on the tight expenditure control the team has seen so far, the IMF is canceling plans it had to bring in a team to assist in expenditure management.

4. (U) Green reported that the team had overestimated inflation in its planning; it now appears that inflation will be 14 to 15 percent at year end, as opposed to the 16-18 percent forecast in July and September. As well, the foreign exchange inflows have been higher than projected, owing to an increase of \$40 to \$60 million in tobacco revenues over last year. Forex reserves now stand at 1.7 months in the central bank.

DONOR CONCERNS

5. (SBU) Donor representatives raised three concerns at the first IMF meeting: that the GOM might decide to break its budget in spending on a new building for Parliament, that the civil service wage reforms could be so unpopular as to spur a free-spending remedy, and that the IMF might be pressing the Reserve Bank to raise interest rates. On the parliament building, Green said the IMF is not concerned, because any new building would take several years to construct, and thus poses no immediate danger to the budget. The civil service pay issue is "more worrisome" according to Green, and "if it's a budget buster, then that's a problem." Green did note that the IMF has always seen the wage reform as difficult, and that it was confident that the issues could be successfully worked through. (NOTE: Finance Minister Goodall Gondwe acknowledged that the GOM miscalculated the net effect of the wage package, and that settling government workers' concerns about a net decrease in take-home pay would be easily resolved, with little effect on the budget. End note.) On interest rates, the IMF position is that the RBM should raise rates only if inflation begins to rise.

NEXT STEPS

16. (U) Under the current SMP, the IMF will continue to monitor performance with quarterly assessment missions. The next mission will come in mid-February to look at performance through the end of December. According to Green, in the best case IMF would negotiate a new PRGF to take effect from 1 April.

COMMENT

17. (SBU) The initial IMF briefings accord with our view of the GOM's performance since May. While it is still distinctly possible that the situation may break down as it has in the past, the current Government seems to understand the importance of establishing a culture of fiscal responsibility and re-establishing its good name with international financial institutions. Indeed, Gondwe has cautioned donors against prematurely celebrating the success of fiscal reforms, saying the GOM still has plenty of work ahead of it. Meanwhile, USG support, via the Millennium Challenge Account's Threshold Program, can help boost precisely the same areas that both the IFIs and the Government have identified as central: fiscal policy and control of corruption.

GILMOUR